



LIGHTHOUSE BEACON

A Guide in the 21st Century

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Lighthouse Investment Commentary

Despite the Skeptics, Market Resurgence is for Real

It's clear now. The long bear market for stocks ended just about a year ago, in October 2002.

With the Standard & Poor's 500 Index up 13.2% through the first nine months, 2003 is shaping up to be a very good year. Yet the skepticism remains.

Certainly, it is easy to understand the caution of the many investors who still feel the pain from the almost three years in which stock prices seemed to only go down. Many investors are reluctant to get back into the market. And some pundits and observers are encouraging doubts about the continued viability of the market recovery.

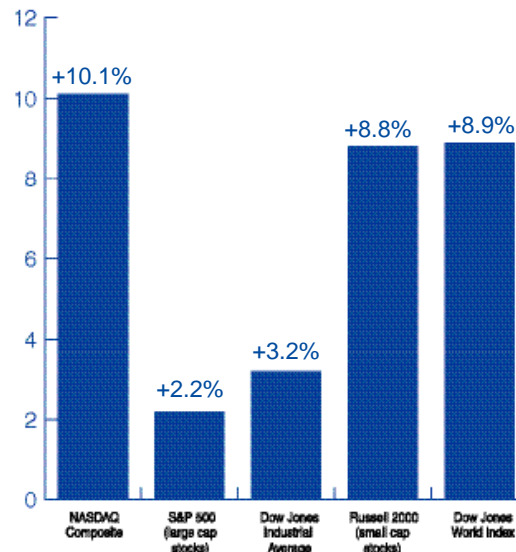
Despite the preponderance of encouraging news and positive indicators about the outlooks for both the overall economy and corporate profitability, many in the media seem to want to continue to concentrate primarily on the few negatives.

We have almost a reverse image of the late 90s when media commentators felt nothing could go wrong. Now, they imply nothing can go right. Just look at the reaction in late September, when the latest report on consumer confidence came in a bit lower than expected.

It has become almost a law of investing that all bull markets climb a wall of worry. There are always some observers trying to find something to worry about, warning about impending gloom and doom even as the markets move higher and higher.

Focus on the Markets

The numbers tell the story. Buoyed by increasing evidence that the economy is recovering, stock markets moved higher in the third quarter of 2003, continuing a resurgence that began one year ago.



This rally is well founded. The economy is picking up strength, corporate revenues and profits are exceeding expectations, and inflation and interest rates remain at historic lows.

Index returns are for price only, and do not include reinvestment of dividends. Past performance is not a guarantee of future results.

In our past two newsletters, we pointed out the many reasons that equities should be moving higher. Let's take another quick inventory of the forces driving stock prices up:

- Faster-than-expected economic growth;
- Rising industrial output, led by technology;
- Improving productivity;
- Improving business confidence;
- Corporate earnings and cash flow exceeding estimates;
- Rising family incomes and increasing consumer spending;
- Higher business spending on both technology and non-technology investments;
- Lower inflation than we have seen in 37 years;

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- Short-term interest rates at a 45-year low, thanks to an accommodating Federal Reserve;
- Tax law changes that include shareholder-friendly reductions in both income tax and capital gains tax rates;
- An increasing number of corporations either introducing stock dividends or increasing existing dividends;
- A strong housing market;
- Falling energy prices.

Phew! That's quite a list.

The one real negative is the lack of new job creation. (See our discussion in *Lighthouse Guides* below.)

With all this evidence, it is no surprise that there are few sellers of stocks on the stock market. Just look at the volumes: on the days the market rises, volume is heavy; on the days the market dips, volume is light.

The skeptics answer that the market

Lighthouse Highlights

Selected Lighthouse Portfolio Holdings Third Quarter 2003 Performance

<u>Company</u>	<u>Sector</u>	<u>Price Change*</u>
Countrywide Financial	Financial	+12.5%
Intel	Technology	+32.7%
Staples	Consumer	+30.0%
Motorola	Telecom	+26.7%
Texas Instruments	Technology	+29.5%
S&P 500		+2.2%
NASDAQ		+10.1%

* Price change only. Neither company nor index returns include any dividends. Performance of individual stock holdings in portfolios managed by Lighthouse Asset Management are not intended to indicate future results.

has come too far, too fast. But has it? We are coming off a three-year bear market. Even after rising 33.8% in the first nine months of 2003, the NASDAQ Composite still is 65% below the heights it reached in 2000.

We now have seen positive results in three of the past four quarters. (The only

negative return occurred during the first quarter of 2003, when the market was embroiled in geopolitical issues, including Iraq and North Korea.) In fact, over the past 12 months, the S&P 500 is up 17.5% and the NASDAQ is up 47.2%.

Now, things look positive from business, financial and economic points of view. In fact, the outlook appears better than we have seen in many years.

As investors, we need to make sure we are not held hostage by our most recent trauma. Without a doubt, the bear market of 2000, 2001 and 2002 was painful. But we cannot allow the memory of that pain to impair our judgment and prevent us from taking advantage of the opportunities we now are seeing.

This is a time that will reward those who are patient and persevering. It is up to us to take advantage of the opportunity!

The views in the Lighthouse Beacon's investment commentary are those of the professional staff of Lighthouse Asset Management, LLC. Our professionals each have more than three decades experience in the capital markets. The team includes: James R. McCall, CFA, President; Dana P. Blake, Jr., Executive Vice President; and Frank H. Gorke, Jr., Senior Vice President.

Lighthouse Guides

Q: If the economy is strengthening, why is job growth so anemic?

A: The slow growth in employment is a negative component of the gains we have made in productivity. In the 1990s, American corporations made significant investments, especially in technology, to improve their operational efficiency and the productivity of their employees. Now, in the initial phase of an economic recovery, those gains in efficiency and productivity are allowing corporations to do more business without significant additions to their workforces. Employment always has been a lagging indicator of the direction of the economic cycle, and it remains so today.

While the service sector is creating jobs, the manufacturing sector is moving more cautiously after being hard hit in the recent recession. That will change when manufacturing companies grow more confident about the sustainability of their improving businesses.

Sales are increasing, corporate profits are improving and stock prices are rising. Employment will follow.

Lighthouse Guides is a regular column answering typical questions posed by clients discussing their portfolios.

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